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ABSTRACT

Bundling, a practice which has increased dramatically in the television and cable industries in recent years, occurs when program distributors package groups of movies and episodes of series, and then sell licenses to use these packages to TV stations and cable channels. Typically, such bundled packages include both highly desirable and less desirable films or episodes of off-network series. Bundling can easily turn into block booking, the illegal practice of making programming available in indivisible units that harm competition. Litigation continues to occur in the motion picture industry as a result of block booking and is beginning to occur in the cable industry, where it is often called "tying." Tying occurs when a programming service requires a system to take an unwanted channel to attain a desired channel; litigation is being directed at services tying cable programs, motion picture studios, and cable operators. Such practices limit the ability of programmers to negotiate prices based on the economic forces of supply and demand. As a result, many stations are forced to pay higher prices for products they would prefer to reject. In addition, bundling and block booking limit the ability to bargain for discounts for using programming in several markets in which a broadcaster may own properties and to barter advertising time for programming. With mergers such as that of Time and Warner Communications creating vertical integration in the programming industry, the linkages of program production, distribution, and exhibition grow stronger and provide more incentive for distributors to engage in economic practices that disadvantage local firms who provide delivery to audiences. (NKA)

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MANAGEMENT AND ECONOMIC IMPLICATIONS OF BUNDLING AND BLOCK BOOKING OF TELEVISION AND CABLE PROGRAMMING

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MANAGEMENT AND ECONOMIC IMPLICATIONS OF BUNDLING AND BLOCK BOOKING OF TELEVISION AND CABLE PROGRAMMING

Bundling of programming has increased dramatically in the television and cable industries in recent years and creates conditions in which anticompetitive practices that harm television stations and cable operations can occur. The bundling, or packaging of groups of programs, now encompasses not only feature films licensed for broadcast and cable use, but also off-network and first-run syndicated programming as well.

In its simplest form, bundling occurs when program distributors package groups of movies and episodes of series, and then sell licenses to use these packages to television stations and cable channels. The practice first emerged in the television industry when motion picture distributors put together packages of feature films for broadcasting use. It was not until later, when independent stations created a post-network market, that packages of episodes of off-network series were created. Typically, such bundled packages included both highly desirable and less desirable films or episodes of off-network series.

In recent years, motion picture packages have grown smaller and distributors have sometimes added off-network series to these packages, thus inducing television programmers to purchase both the motion pictures and series, even if they only wanted the films or the series. This has compounded the problems created by

commodity bundling that are faced by television and cable program directors and it creates managerial, economic, and legal problems for the television and cable industries.

Bundling can easily turn into block booking, the illegal practice of making programming available in indivisible units that harm competition. The line between permissible and inpermissible bundling is finely drawn. Block booking occurs when groups of films or programs, or films or programs, are offered only as a bundled package. As a result, most distributors provide means of purchasing products individually but at prices that provide disincentives to do so. However, if the price schedules are intended to harm those who wish to purchase products individually, and are anticompetitive to the point that they become coercive, such bundling then becomes block booking as well.

Development and Outlawing of Block Booking

Block booking emerged first in the motion picture industry when studios required theater operators to purchase blocks of films to exhibit in their theaters. The practice was found to violate antitrust laws in 1948 in U.S. v. Paramount Pictures Inc.1 The court provided the standard definition of blook booking:

> The practice of licensing, or offering for license, one feature or group of features, upon condition that the exhibitor also take a license for another feature or group of features released by the distributor during a given period.2

In a consent decree developing out of the 1948 case, all the major motion picture studios agreed not to engage in future block booking under penalty of criminal contempt and fine.

Roy Kenney notes that the antitrust sanctions against block booking increase costs for distributors and exhibitors because the exhibitors must make choices about goods of uncertain and unequal quality. As a result, distributors increase promotional and informational activities, at a corresponding cost, to provide more information to exhibitors. Exhibitors likewise increase their costs by seeking and acquiring information about the type and quality of productions offered.3 The anticompetitive harm of block booking on the market, however, has led antitrust officials and courts to consider that harm to be more significant than the added costs incurred by distributors and exhibitors.

The prohibitions on illegally tying media products did not end bundling practices, however. When television programmers began significantly using motion pictures, both permissible bundling and blook booking appeared in sales of motion picture packages to stations. Block booking in licensing of motion pictures for television was found to be anticompetitive in 1962 in U.S. v. Loews Inc., based upon the decision in the Paramount Pictures case.4

George Stigler argued that the 1962 decision, although consistent with case law, did little to change market forces.

> The effect of the decision, if it is effective, is to reduce the receipts of the owners of the films, and to increase the receipts of another set of monopolists, the owners of TV licenses. If the TV licenses were sold by the government, the redistribution would be beneficial; as it stands, no clear judgment seems possible.5

Despite such arguments, efforts to halt block booking in television have continued and have resulted in litigation and an inquiry by the Antitrust Division of the U.S. Department of Justice into package deals involving syndicated off-network television programs. These actions convinced an industry legal expert to note in 1981 that

> block sales--sales of a number of movies as a package to television--have led to many abuses in the industry. Distributors often lumped a highly lucrative film with unsuccessful ones, and allotted the over-all price to the prejudice of the profitable one. The practice has been exposed; most pictures are now individually offered and individually priced.6

Despite his optimism and consistent rulings against block booking practices, the tying of products and the conditions for abuse of that bundling continued. In 1982, an antitrust suit brought against NBC and syndicated programming purchasers by the producers of the programs "Bonanza" and "High Chaparral" contended that the producers were harmed when television stations were forced to buy other programs in order to get the desirable westerns. A court of appeals ruled that producers could claim injury if violations were proven, thus broadening the definition of who has standing in disputing block booking arrangements.7

The practice of bundling has continued despite high litigation costs and judgments against distributors for block booking. Programming packages are now well established in the television and cable industries industry in the licensing of syndicated programming and films.8

Although blook booking is clearly illegal, litigation and judgments against blook booking continue to occur, with one of the most recent being a $500,000 fine levied against Twentieth Century Fox for blook booking "Space Camp" and "Aliens" and "Prizzi's Honor" and "Cocoon."9 Several lawsuits against film and television programming producers and distributors--including Twentieth Century Fox--for block booking are currently in the courts.

Entertainment law experts Thomas D. Selz and Melvin Simensky argue that the continuance of book booking is not surprising because of the costs and risks of motion picture production:

> The incentive to engage in block booking is obviously to increase the chances for survival in the huge investment/high risk atmosphere of the industry. The increased chances may occur directly, as a result of greater revenues for projects which have not attracted a mass audience, or indirectly, as a result of alleged allocations with less cash outlay. A direct relationship between block booking and an increased chance for survival occurs because well-received productions (the tying product) help generate sales for less successful ventures (the tied product) which otherwise would not be earning anything, or would be earning less, toward the cost of their production and distribution."10

Although there may be some rationale for this argument in the motion picture industry alone, it does not account for block

booking of television programming where economic risks for producers are relatively low because many productions are funded by the network purchasers. The continuance of bundling and block booking in the licensing of motion pictures to television is probably better attributed to the low risk and high profit of doing so made possible because enforcement by antitrust authorities has been lax in recent years, and few television stations are willing to pay the costs of challeging questionable pricing practices in court.

Although television programming and motion picture distribution contracts and relationships differ, William Jennings argues that the practices of network television distribution constitute block booking and that the use of such practices reduces costs in the same manner described by Kenny.11

Bundling is also found in the provision of cable programming, where it is often called tying. "Tying occurs when a programming service requires a system to take an unwanted channel in order to obtain a desired channel," according to cable law specialist Ira Stein.12 The practice is often promoted by price arrangements that tie channels together and provide significant cost advantages to cable systems when more than one channel is purchased from the same programming supplier, such as Turner Broadcasting System or Home Box Office. A downstream bundling of services occurs when cable operators create packages of channels for consumers that provide a group of channels, including wanted and unwanted channels, in basic and premium packages.

Such activies are beginning to result in litigation in the cable industry that cites block booking prohibitions on bundling for anticompetitive purposes. Litigation is being directed at services tying cable programs, motion picture studios, and cable operators.

Implications for Television and Cable Managers

The presence of bundling and block booking present significant problems for television station and cable system managers because it makes them vulnerable to litigation from producers and subscribers for creating and promoting packages, as well as for collusion or price fixing. It also significantly disadvantages them in negotiations and when making programming choices.

When stations are consumers of programming, bundling and block booking economically favors program producers and distributors by limiting the abilities of stations to choose programming that will allow them to program effectively against local competitors.

The major difficulty is, of course, the anticompetitive effects of these practices in limiting the operation of the marketplace. These practices limit the ability of programmers to negotiate prices based on the economic forces of supply and demand. As a result, many stations are forced to pay higher prices for products than is warranted and to accept products they would prefer to reject. In addition, bundling and block booking limits the ability to bargain for discounts for using programming

in several markets in which a broadcaster may own properties and to barter advertising time for programming.

In pure block booking, no negotiations over programming are typically permitted in the acquisition of block products. Broadcasters must acquire all the materials in the package or they get none of the products. Stations are clearly at a disadvantage in this situation because the market power disparity of the distributors with desirable products is sufficient to coerce broadcasters to sign contracts that include poorer, unwanted products. Even when bundling that permits some purchases out of the packages exist, it is usually so diseconomic as to present the same problem.

Bundling creates a variety of other problems that are in many ways more important to the financial well-being of individual television stations. First, the practice creates significant financial pressures on stations by contributing to overbooking and acquisition of unwanted product. Broadcasters who may need a group of films for a prime time movie schedule may also be forced to accept a situation comedy or dramatic series for which they have no need or available time. This increases a broadcaster's programming costs, especially if the station must warehouse a product rather than use it.

The rising costs of programming generally in the early 1980s, along with forced acquisitions through block booking, have probably played a role in the faltering financial condition of some television stations. Since the mid-1980s, nearly two dozen

stations have declared bankruptcy, an unheard of development in the television industry in previous years.

Bundling and block booking also have damaging programming effects in that they limit the counterprogramming strategies of broadcasters, thus reducing their flexibility. This disadvantages stations both competitively and financially in their local markets. A station, for instance, may face a competitor that is broadcasting situation comedies during prime access time. If the station has been forced to acquire an unwanted situation comedy--"Sanford and Son," for example--as a result of bundling, the management may be forced to use it and other comedies, duplicating the strategy of the other station, rather than counterprogramming through acquisition of reality-programming such as "A Current Affair," or courtroom series, such as "Superior Court."

Network affiliates can be especially harmed by bundling and block booking because they have far less time to use for programming purchased from distributors. Most affiliate stations have only about a third of their broadcast time available for non-network programming. If they are forced to purchase unwanted programming in packages, they have very limited time blocks during which to utilize all the programming and thus are more likely to be forced to warehouse unwanted purchases.

The practice also artificially lowers the product quality of stations by forcing poorer programs and movies into the schedule, practices that are damaging in marginally competitive markets but

can be devastating in markets with many broadcast stations and readily available cable competition. Bundling of motion pictures for television usually results in stations purchasing packages with a few desirable films, some acceptable films, and a few undesirable films. This presents the fewest management problems of the various forms of block booking encountered by television managers. If the films are scheduled for a regularly occurring time slot, the audiences generated by each motion picture can be expected to reasonably equalize over time, so that the impact of any given film that is broadcast does not affect advertising significantly. If a package contains a few undesirable films, the program manager can also choose not to air these products and to replace them with other films. If the film package is reasonably large, the cost of such substitution can be average among the films aired and have only a minor impact on overall programming costs.

Bundling and block booking can also force programmers into "checkerboarding" in order to use all the material. This practice involves rotating a variety of programs in a single time slot, but it has been a failure at generating significant audiences in prime access time and has been generally unsuccessful in other time periods as well.

The creation of program packages is beginning to create friction between television and cable programmers as competition between the two industries for viewers increases. This tension emerged at the 1989 National Associaton of Television Program

Executives (NATPE) meeting when television programmers complained to motion picture syndicators about films packages being sold to both broadcast stations and cable channels and pressured syndicators to stop agreements to sell cable windows for major movie packages.13

As practices, bundling and block booking are akin to the practice that can be euphemistically called the "Cuba Libre" approach to purchasing of alcohol during Prohibition and the Second World War. During these periods, when the availability of liquor was limited by law and shortages, a buyer of liqour would be forced to purchase poor quality rum in order to get better quality liquors. The practice ultimately led to the rise of popularity of the Cuba Libre, a rum and cola drink, because the cola masked the flavor of the poor quality rum. Whether the tying of these commodities was illegal or not, the scarcity and desirability of the premier product kept most consumers happily paying the diseconomic cost of the bundled products. The analogy works well with television and cable programming because the product is also scarce and in high demand.

Today, bundling in television and cable programming involving motion picture packages and off-network programming includes groups of episodes currently released for syndication, episodes already aired but not yet available in syndication, and sometimes future episodes to be produced even if they are not aired on networks.

Paramount Pictures, for example, recently offered

programmers Portfolio XIII, a motion picture package consisting of such films as "Top Gun," "Crocodile Dundee," and "The Untouchables." Some distributors have allegedly tied film packages to television programming, such as linking packages of programs such as "Who's the Boss?" or "One Day at a Time" to purchases of films. In addition, syndicated off-network and first-run programming are also being tied. TV Horizons, for example, has a package consisting of episodes of the original network "Giget" and "New Gidget" shows.

Programmers have made few responses to the difficult position in which they have been placed by distributors' practices. Organized industry efforts to halt such practices have not occurred and, in fact, most television industry associations have no policies and have take no positions reqarding the practice. Even the National Association of Broadcasters, the Association of Independent Television Stations, and the National Association of Television Program Executives have not officially addressed the problems that the practices pose their members, reflecting the general opinion that there is little that can be done about the situation and that it must be accepted and endured.

Ignoring the issue, however, opens individual television television station and cable system operators to potential charges of collusion and leaves them to individually face the greater power of the program distributors. In order to protect members against lawsuits and competitive and economic harm that

can result from both bundling and block booking, these industry organizations may need to organize pressure or litigation or their own, or ask the U.S. Department of Justice to more stringently police the practices involving their industries.

The need for concern about bundling and block booking practices is increasing daily and major film and television program producers move even more heavily into distribution and exihibiton aspects of cable and the competition between television and cable increases. The merger of Time Inc. and Warner Communications and the vertical integration it creates in the programming industry, as well as continued vertical and horizontal integration of firms such as Tele-Communications, Inc. (TCI) and United Artists Entertainment Co. can be expected to pose significant problems for television broadcasters and cable operators as the linkages of program production, distribution, and exhibition grow stronger and provide even more incentive for distributors to engage in economic practices that disadvantage local firms who provide delivery to audiences.

NOTES

1. United States v.Paramount Pictures, Inc., 66 F. Supp. 323 (D.C. N.Y. 1946); mod. 70 F. Supp. 53 (D.C. N.Y. 1947); 334 U.S. 131 (1948); remanded 85 F. Supp. 881 (D.C. N.Y. 1949); affirmed against appellants 339 U.S. 974 (1950).

2. 66 F. Supp. 323 (D.C. N.Y. 1946).

3. Roy W. Kenney, "The Economics of Block Booking," Ph.D. Dissertation, Economics Department, University of California, Los Angeles, 1979.

4. Unites States v. Loews, Inc., 189 F. Supp 373 (SD N.Y. 1960); 371 US 38 (1962).

5. George J. Stigler, "A Note on Block Booking," in The Organization of Industry (Homewood, Ill.: R. D. Irwin, 1968), p. 169.

6. Alexander Lindey, Lindey on Entertainment Publishing and the Arts 3 vols. (New York: Clark Boardman Co, 1981), V. 2, p. 883.

7. Aurora Enterprise v. NBC, 524 F. Supp. 655; 688 F. 2d 689; 52 RR 2d 693 (1982).

8. Susan Tyler Eastman, Sydney W. Head, and Lewis Klein, Broadcast/Cable Programming: Strategies and Practices 3rd ed. (Belmont, Calif.: Wadsworth, 1989).

9. Al Delugach, "20th Century Fox Fined $500,000 in Booking Dispute," Los Angeles Times, December 8, 1988, Sec. IV, p. 1.

10. Thomas D. Selz and Melvin Simensky, Entertainment Law: Legal Concepts and Business Practices (Colorado Springs, Co.: Shepard's/McGraw Hill, 1983), Sec. 5, pp. 8-9.

11. William P. Jennings, Jr. "An Economic Analysis of the Use of Block Booking Among Motion Picture Distributors and the Television Networks," Ph.D. Dissertation, Economics Department, University of California, Los Angeles, 1981.

12. Ira C. Stein, Cable Television: Handbook and Forms (Colorado Springs, Colo.: Shepard's/McGraw Hill, 1985), pp. 11-23.

13. Wayne Friedman, "Cable's NATPE Flap," Cablevision, February 13, 1989, p. 13.